DOMTAR

ANNUAL REPORT
1972
DOMTAR LIMITED

CONTENTS

The annual meeting of Domtar Limited will be held Thursday, April 26, 1973 at 4 p.m. in the Windsor Hotel, Montreal, Quebec.

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HIGHLIGHTS

	1972	1971
Sales	$560,779,334	$516,376,401
Income taxes — Current	$ 8,320,000	$ 4,550,000
Income taxes — Deferred	$ 5,255,000	$ 4,430,000
Net income before extraordinary items	$ 17,467,787	$ 10,500,439
Net income after extraordinary items	$ 13,367,787	$ 1,800,439
Common shares outstanding	14,827,300	14,827,300
Earnings per common share before extraordinary items	$ 1.14	$ 0.67
Earnings per common share after extraordinary items	$ 0.86	$ 0.08
Dividends per common share	$ 0.60	$ 0.60
Working capital	$130,239,101	$124,220,727
Cash flow — Total	$ 49,580,427	$ 41,037,488
Cash flow — Per common share	$ 3.30	$ 2.73
Expenditures on fixed assets	$ 28,485,046	$ 23,655,786
Book value per common share	$ 15.63	$ 15.37
Number of preference shareholders	1,825	1,775
Number of common shareholders	34,824	39,027
Number of employees	17,436	17,607
Payroll and Benefits	$175,422,000	$167,364,000

DIRECTORS AND OFFICERS

Directors

*Alex E. Barron, Toronto,
Chairman of the Board, Canadian Tire Corporation Limited

*T. N. Beaupré, Montreal,
Chairman of the Board and President, Domtar Limited

*H. Roy Crabtree, Montreal,
Chairman and President, Wabasso Limited

J. E. L. Duquet, Q.C., Montreal,
Senior Partner in the legal firm of Duquet, MacKay, Weldon, Bronstetter and Johnston

*A. L. Fairley, Jr., Birmingham, Ala.,
President and Chief Executive Officer, Hollinger Mines Limited

C. L. Gundy, Toronto,
Chairman, Wood Gundy Limited

Roger T. Hager, Vancouver,
Chairman of the Board, The Canadian Fishing Company Limited

Alex D. Hamilton, Montreal,
President, Domtar Pulp & Paper Products Ltd.

J. G. Kirkpatrick, Q.C., Montreal,
Partner in the legal firm of Ogilvy, Cope, Porteous, Hansard, Marler, Montgomery & Renault

Camille Lacroix, St. Romuald, Quebec,
President, Matapedia Company Limited

Roger Létourneau, Q.C., LL.D., Quebec,
Senior Partner in the legal firm of Létourneau, Stein, Marseille, Delisle & LaRue

*A. Bruce Matthews, C.B.E., D.S.O., Toronto,
Chairman, The Excelsior Life Insurance Company

*John A. McDougald, Toronto,
Chairman and President, Argus Corporation Limited

*Maxwell C. G. Meighen, O.B.E., Toronto,
Chairman of the Board, Canadian General Investments Limited

Nathan Pitcairn, Jenkintown, Pa.,
Director, Pitcairn Incorporated

*Arthur Ross, New York,
Executive Vice-President and Managing Director, Central National Corporation

*J. N. Swinden, Toronto,
General Manager, Argus Corporation Limited

J. Thomas Timmins, Montreal,
President, Chromasco Corporation Limited

*Colin W. Webster, Montreal,
Vice-Chairman of the Board, Canadian Fuel Marketers Ltd.

*Members of the Executive Committee

Les actionnaires qui préféreraient recevoir leurs rapports en français voudront bien en aviser le Secrétaire de Domtar Limitée

Officers

T. N. Beaupré,
Chairman of the Board and President

S. A. Kerr,
Vice-President — Administration and Secretary

J. P. Lunderville,
Vice-President — Engineering, Purchasing and Transportation

R. J. Moyse,
Vice-President — Finance

G. H. Tomlinson,
Vice-President — Research and Environmental Technology

G. M. Drodge,
Controller

C. A. Brooke,
Treasurer

E. G. Aust,
Assistant Treasurer

A. Gascon,
Assistant Secretary

Operating Companies

Domtar Chemicals Limited
President — A. Monsaroff

Domtar Construction Materials Ltd.
President — J. Cochran

Domtar Pulp & Paper Products Ltd.
President — A. D. Hamilton

Domtar Fine Papers Ltd.
Vice-President and General Manager — J. H. Robertson

Domtar Newsprint Limited
Vice-President and General Manager — W. D. Davidson

Domtar Packaging Limited
Vice-President and General Manager — W. R. Lawson

Domtar Pulp Limited
Vice-President and General Manager — R. R. Pinard

Domtar Woodlands Limited
Vice-President — A. S. Fleming

Head Office

395 de Maisonneuve Blvd. West,
Montreal 111, Que.

Transfer Agents

for preference and common shares:
Montreal Trust Company — Halifax, N.S.; Saint John, N.B.; Montreal, Que.; Toronto, Ont.; Winnipeg, Man.; Regina, Sask.; Calgary, Alta.; Vancouver, B.C.

for common shares only:
The Bank of New York — New York, N.Y.

Registrars

for preference and common shares:
The Royal Trust Company — Halifax, N.S.; Saint John, N.B.; Montreal, Que.; Toronto, Ont.; Winnipeg, Man.; Regina, Sask.; Calgary, Alta.; Vancouver, B.C.

for common shares only:
The Bank of New York — New York, N.Y.

REPORT OF THE DIRECTORS TO THE SHAREHOLDERS

The consolidated financial statements of Domtar Limited and its subsidiaries for the year ended December 31, 1972 and the report of the Auditors are submitted on behalf of the Board of Directors.

Sales and Profits
Sales and profits for the year 1972 reflected the more buoyant economic conditions which prevailed during that year. Sales, cash flow and net income were all appreciably higher than in 1971. While sales were up 8.6% and cash flow 20.8%, net income before extraordinary items rose by 66.4%.

Net income before extraordinary items amounted to $17.4 million or $1.14 per common share compared with $10.5 million or 67 cents per common share in 1971. Cash flow reached $49.6 million, the highest amount since 1965.

Sales during 1972 compared with the previous year were distributed among the three major product groups as follows:

	1972		1971	
	$ millions	%	$ millions	%
Pulp & Paper	364.5	65.0	338.5	65.6
Construction Materials	110.9	19.8	97.7	18.9
Chemicals	85.4	15.2	80.2	15.5
	$560.8	100.0	$516.4	100.0

Sales and operating profits in the Pulp and Paper group increased substantially although the return on investment remains inadequate. By far the largest portion of the profits of this group was earned by Packaging and Fine Papers and the financial results from Newsprint showed an appreciable improvement. While the operations of the pulp mill and chemical plant at Lebel-sur-Quévillon, Quebec, made a slight contribution to cash flow, they did not add to the operating profits of the Company.

The marked improvement in the building industry, especially in the housing sector, had a most favourable effect upon the income generated by the Construction Materials company.

Although the profits of the Chemicals group were not up proportionately as much as those in the Pulp and Paper and Construction Materials companies, they again made a most significant contribution to the consolidated results of Domtar Limited.

Extraordinary Items
In line with its policy of continually reviewing the viability and profitability of its various operations and facilities with the aim of eliminating or altering those which have not added and are not expected to add to the financial results of Domtar Limited, the Company decided to close down the Siporex plant at Delson, Quebec. Following an explosion which partially destroyed its metal powders plant at Ridgway, Pennsylvania, in early September 1972, the Company has put the facilities up for sale; the plant has not been in operation since the explosion.

In addition, certain non-recurring costs related to severance pay and the retraining of personnel were incurred in connection with the closing of these two plants and these amounts have been included in the extraordinary items.

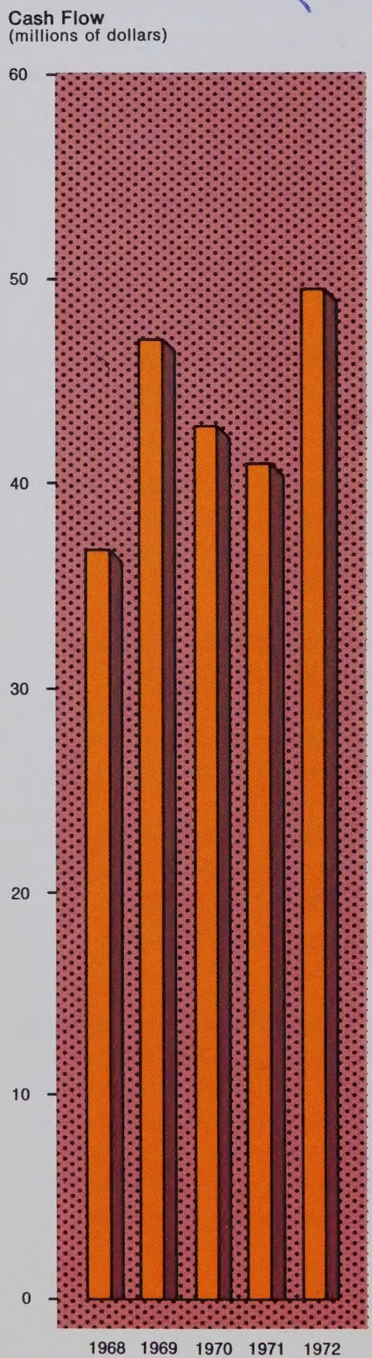
The Company has also decided to write off certain equipment which is idle and of no further use in the linerboard and newsprint mill at Red Rock, Ontario.

As a result of these decisions, extraordinary items amounting to $4.1 million were charged against profits, reducing net income to $13.3 million or 86 cents per common share. Cash flow was not materially affected.

Losses incurred by facilities taken out of operation during the year had the effect of reducing the year's earnings by about 11 cents per share.

Taxes
Due to higher earnings, current income taxes charged against profits were $8.3 million in 1972 compared with $4.6 million the previous year. Current income, municipal, school and capital taxes amounted to $16.5 million in 1972. It is disturbing to note that municipal, school and capital taxes have risen from

Capital expenditures



$5.2 million in 1964 to $8.2 million in 1972 or, put another way, from 11% of profits before deducting these taxes and income tax in 1964 to 21% in 1972. School, municipal and capital taxes are fixed charges against earnings; the amount paid does not depend upon the level of profits.

Funded Debt

In April 1972, the balance of $7.1 million owing on the 5% Series "A" and the 4¾% Series "B" first mortgage sinking fund bonds of St. Lawrence Corporation Limited, which appeared in current liabilities at the end of 1971, was repaid. The total funded debt outstanding at the end of 1972 including that portion due within one year amounted to $123 million compared with $134.2 million at the end of 1971, a reduction of $11.2 million.

Fixed Assets

Net expenditures on fixed assets amounted to $28.5 million. Aside from outlays for pollution abatement, the major projects included the expansion of corrugating facilities in the Toronto area and of the salt mine at Goderich, Ontario, the increase in capacity of the tar products plant in Hamilton, Ontario, and the profit improvement program in the linerboard and newsprint mill at Red Rock. Approximately $40 million is expected to be spent on fixed capital additions and related investments in 1973.

Working Capital

The net working capital ratio of 3 to 1 at the end of 1972 was the same as at the close of the previous year.

The liquid position of the Company measured by the "quick assets" (cash and short-term investments and receivables less all current liabilities) continued to remain strong with quick assets amounting to $43.3 million. Although substantial sums were spent on debt retirement and were invested in fixed assets and operating working capital, the net cash position of the Company (cash and short-term investments less bank indebtedness), was $9.8 million at December 31, 1972 compared with $9.4 million at the end of 1971.

Minority Interests

At the end of 1972, the Company held 98.8% of the common stock of St. Lawrence Corporation Limited, which in turn owned all but 144 of the 360,000 issued common shares of Hinde and Dauch Limited. Only 15 out of the 486,000 outstanding common shares of Buntin Reid Paper Co. Limited were held by minority interests. The Company still retains its 51% ownership of Chemical Developments of Canada Limited with GAF Corporation of New York holding the balance.

Source and Application of Funds

Over the past five years, 1968 through 1972, the Company generated a cash flow of $218 million, spent $126 million (net) on fixed assets, reduced the long term debt by $42 million, invested $12 million in additional working capital and disbursed $46 million in the form of dividends to the common shareholders.

Labour Relations

Fifty-four collective agreements were negotiated during the year. Eight strikes occurred with a resultant loss of 18,642 man-days.

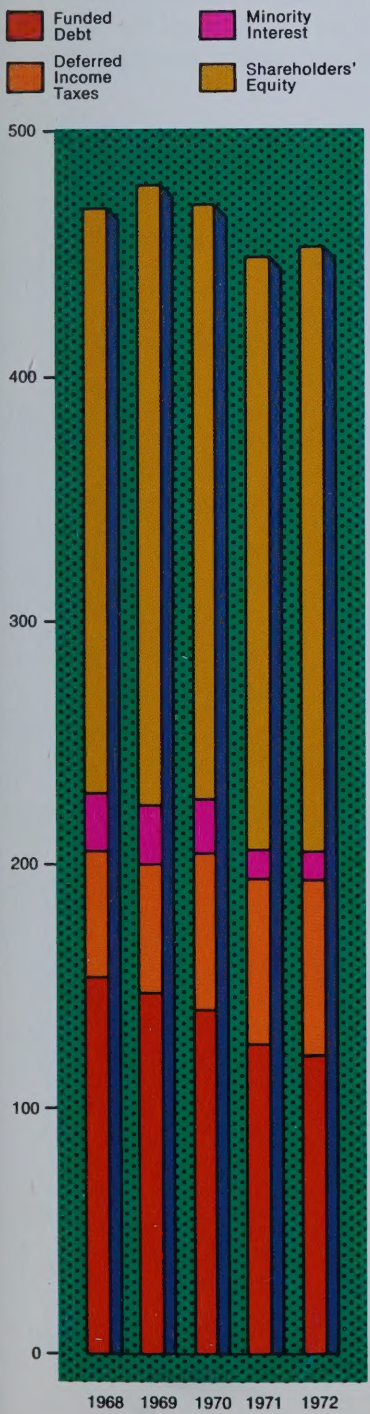
The bargaining process continues to be protracted and crisis-oriented with only 16 out of 54 settlements reached in direct negotiations without resorting to government conciliation services.

The rationalization of production facilities in line with current market demands for the Company's products regretfully resulted in complete or partial plant closures at four locations. In all cases, special efforts were made to transfer employees elsewhere in the Company and also to provide extensive counselling services to those whose employment had to be terminated. The negotiated employees affected by the shutdowns are being assisted by action of the Domtar Industrial Conversion Plan.

Personnel Administration

The Company continued its policy of integrating personnel programs with existing social welfare legislation resulting in changes and improvements in employee benefits and

Capital Structure
(millions of dollars)



government-assisted training activities. There was an unfortunate decline in the overall safety record and operating management is taking every appropriate action to correct this situation.

Research

During 1972, the Company continued its extensive research program at the Senneville, Quebec, Research Centre.

Major emphasis has been placed on projects directly related to operations with the aim of increasing profitability, particularly in the areas of cost reduction and of product and process improvement. In addition, considerable effort has been directed towards the development of new products and new processes and a number of these are now in commercial operation or are being considered for production. The Research Department was awarded three contracts by the Federal Government to carry out research on specific projects of mutual interest.

Pollution Abatement

The Company has continued to pursue a broad environmental research program with the object of evaluating the effect of plant effluent on the environment and of developing efficient methods for reducing or treating these effluents in order to conform to Government regulations. Conventional waste treatment techniques have sometimes been found wanting; for instance, treatment of waste waters can sometimes result in secondary air pollution or solid waste problems. Research studies have pointed the way to new directions for dealing with these difficulties and these are now being incorporated into plant projects.

As part of the continuing pollution abatement program, two clarifiers, one at Cornwall, Ontario, and the other at Red Rock, went on line during 1972. An additional clarifier is now under construction at Beauharnois, Quebec, and will become operational in 1973. Attention is also being given to air pollution problems and major installations are now in the engineering and construction phase.

Total capital expenditures for pollution abatement during 1972 amounted to about $6 million or some 20% of capital expenditures.

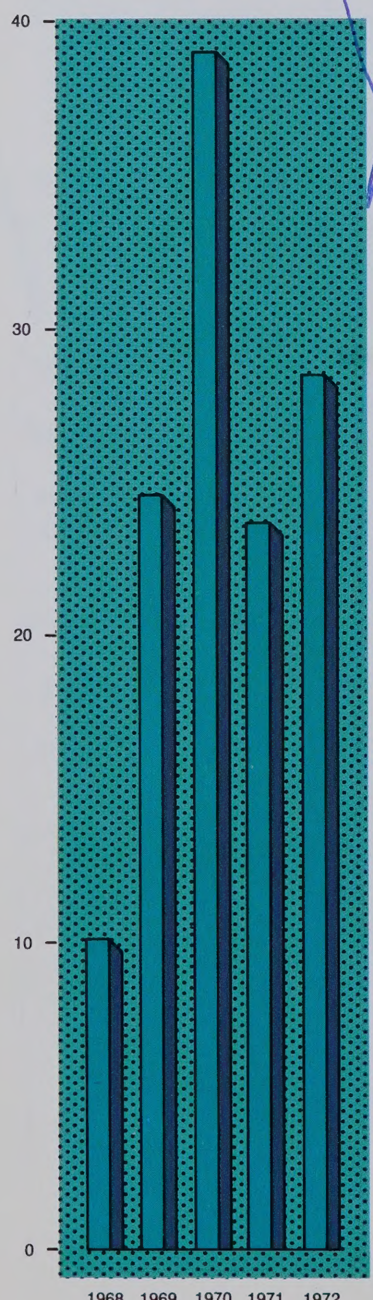
Prospects for 1973

Business activity during 1973 is expected to continue at a high level with appreciable real gains in the gross national product. Inflation remains a cause of major concern. The persistent upward pressure on costs is especially disturbing for those Canadian companies, such as Domtar, which compete in world markets. The unsettled conditions in international monetary and trade relations, particularly those between Canada and the United States, add a new dimension of business uncertainty to the outlook for the year ahead. In addition, on the labour scene, there are 79 collective labour agreements subject to negotiation in 1973; included are those covering all the primary pulp and paper mills in the Company.

Improved financial results are anticipated during 1973 from the Pulp and Paper company. Demand for all products has been increasing. Higher efficiencies, greater output and a more stable level of operations are expected to be achieved in the pulp mill and chemical plant at Lebel-sur-Quévillon. Although competition will remain keen in the markets for fine papers, profits are expected to show a modest gain. As the trend of increasing demand for packaging grades of paper and paperboard and for corrugated containers is expected to continue into 1973 and as added capacity came on stream in late 1972, the sales and profits of the Packaging company should be moderately higher.

High levels of activity are expected to continue in the construction sector of the economy. In 1972, housing starts were at a record level and commercial and industrial building activity gathered increasing momentum as the year progressed. The

Capital Expenditures
(millions of dollars)



supply of mortgage funds appears sufficient to sustain an active building program. While the growth in residential construction achieved during 1972 cannot be expected to continue into 1973, it is anticipated that the level of construction activity as a whole will remain close to that reached in 1972. In this environment, the Construction Materials company is expected to maintain the level of profitability achieved in 1972.

Sales of the Chemical company are expected to grow moderately in 1973. Profit improvement will largely depend upon reducing those costs over which management has control.

In view of the foregoing, the outlook for Domtar Limited is encouraging and improved financial results are expected to be achieved in 1973.

Board of Directors
Due to the Company's policy with respect to an age limit for Directors, Mr. C. W. Webster will not be standing for re-election as a Director at the 1973 Annual Meeting of Shareholders. Mr. Webster joined the Board on February 4, 1952 and served on the Executive Committee of the Board from May 5, 1952 as well as on other Committees of the Board. Particular thanks are extended to Mr. Webster, who participated actively in the affairs of the Company, for his many years of distinguished service.

Late in 1972, Mr. R. W. Cooper tendered his resignation as a Director for reasons of health. The Board has regretfully accepted his resignation. Mr. Cooper had been a Director of Gypsum, Lime and Alabastine, Canada, Limited for many years and joined the Board of Domtar on April 13, 1959 when the business of Gypsum, Lime was acquired. Mr. A. D. Hamilton, President of Domtar Pulp & Paper Products Ltd., was recently elected to the Board to fill this vacancy.

With respect to the second vacancy, it is proposed that the number of Directors be reduced from 19 to 18.

Appreciation
The Board wishes to record its appreciation of the efforts and loyalty of those employees whose cooperation and efficiency in the performance of their duties helped to make possible the improved results for 1972.

On behalf of the Board

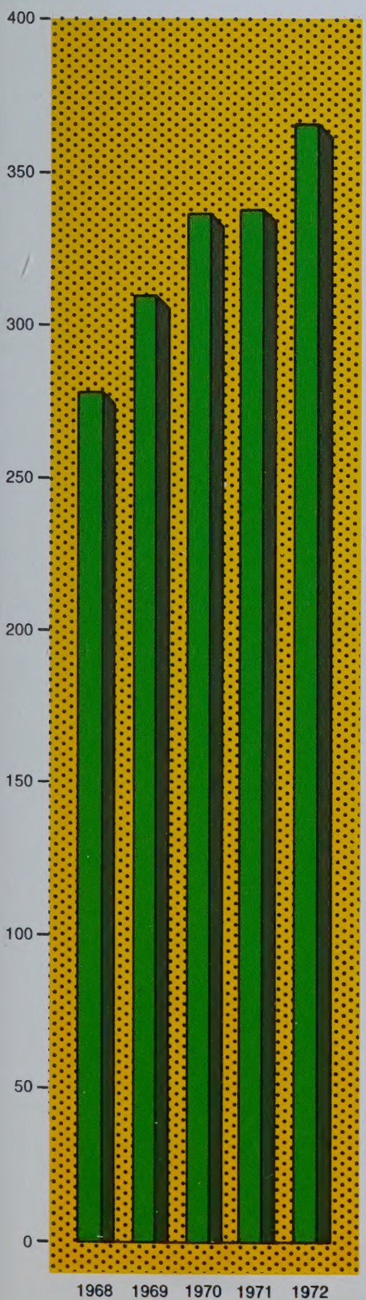
T. N. Beaupré
Chairman of the Board and President

Montreal, Quebec
March 9, 1973.

DOMTAR PULP & PAPER PRODUCTS LTD.

The foreign and domestic operations of Domtar Pulp & Paper Products Ltd. are managed through five major operating divisions: Fine Papers, Packaging, Newsprint, Market Pulp and Woodlands. During 1972, about 68% of the group's sales were made in Canada (primarily Fine Papers and Packaging products), 20% in the United States (mostly Newsprint and Pulp), and 12% in other foreign markets. Our fibre supply is drawn from sources in Ontario, Manitoba and Quebec and encompasses significant quantities of waste paper, sawmill residues, agricultural residue and textile waste as well as pulpwood from privately-owned, leased and government-managed forest lands. However, fibre supply in Eastern Canada, affected by a shortage of labour and poor weather, is a matter of some concern as demand by pulp and paper mills and sawmills has increased substantially.

Pulp and Paper Products Sales
(millions of dollars)



Profits in 1972 increased significantly from the very low level of 1971 with the biggest improvements shown by the Fine Papers, Packaging and lumber operations. The closing-down of four newsprint machines at Trois-Rivières, Québec, at the end of March, 1972 contributed to the improvement in the performance of the Newsprint division and the discontinuance of operations of the sulphite mill and related facilities at Cornwall improved the results of the Fine Papers division. The Market Pulp division continued to be affected by depressed prices and low demand. Operations at the Lebel-sur-Quévillon pulp mill approached design capacity by year-end.

Despite the improvement in profits, the performance of the Pulp & Paper Products company taken as a whole was unsatisfactory as judged by the normal financial tests of return on assets, sales and shareholders' equity. This same situation exists for most of the Canadian pulp and paper industry.

The industry is emerging from a period during which world-wide demand trends flattened out while the trend to increased capacity continued. This situation resulted in reduced operating rates in the Fine Papers, Newsprint and Pulp sectors and inadequate price adjustments to offset the increase in costs. Profit margins during this period were severely reduced. Foreign currency changes accentuated the problem of profit margins, not only for exports but in the Canadian domestic market as imports became very competitive. Cash demands for plant modernization and improvement remained high and demands for pollution abatement expenditures continued to increase.

Domtar Pulp & Paper Products, as well as the industry in general, has been able to improve its organization, its management techniques and its planning and is in a sound position to take advantage of the improved overall supply-demand balance forecast for the next two years. Barring major economic disturbances, it is reasonable to expect that our operations will run very close to capacity in 1973.

However, the company and the industry cannot plan on being able to operate at capacity rates for other than the very short term future. Domtar must establish satisfactory profit margins at less than full capacity to develop the cash flow necessary to permit the continued modernization of the physical facilities and the expansion of facilities where appropriate.

The problems of the Canadian pulp and paper industry have been well publicized over the last two years. There is a danger that these problems may be viewed out of perspective. The industry has endeavored to establish publicly that it can contribute significantly to the Canadian economy but that such contribution can only be achieved through joint efforts of industry, government and labour.

The company believes that the concept of the free enterprise system is the most effective way of creating economic well-being for the Canadian community. We also agree that governments and labour have a major role to play in the industrial development of our country.

The principles of collective bargaining are accepted but the labour statutes should not be unduly weighted in favor of union or management. The responsibility of the unions to the country must be demonstrated by helping to keep Canadian industry costs competitive with foreign companies, particularly in the United States. This can be done by relating monetary demands to factors such as ability to pay, productivity improvements and the ability of the industry to generate sufficient cash to aid in keeping plants modern, efficient and, more important, growing and expanding on a planned basis.

Industry must take responsible decisions for improving its organization, modernizing its facilities, expanding its operations, pricing its products and controlling its costs. Industry must also be more innovative and selective in optimizing markets and improving its product mix; be more skillful in labor negotiations; utilize more effectively technological improvements; and broaden research policy.

These decisions can only be made, however, within an environment which is largely outside the control of industry. It is the federal, provincial and municipal levels of government which must

take the responsibility for establishing a stable, long-term environmental base from which the pulp and paper industry can compete internationally and attract investment capital.

The federal and provincial governments have indicated an awareness of the reality of the factors affecting the industry and have made some revisions in taxation policy at the federal level and in stumpage deferral for approved pollution abatement projects at the Quebec provincial level.

It is against this background that the industry has requested that specific action be taken by governments to review the country's system of transportation costs (the largest single component in the delivered cost of pulp and paper products to customers); consider further revisions to the tax structure; review the overall economic impact of discretionary grants to the Canadian pulp and paper industry; review policies for hydro-electric power rates, stumpage, ground rent and fire protection costs associated with timber licences; and review municipal, school and sales taxes.

In respect to tariff policy, although the trend to freer trade is in the longer term interests of Canadian industry, the governments concerned should make haste slowly and ensure that any adjustments to tariffs are accompanied by policies which will permit the domestically-based operations of the Canadian industry to compete equitably with international competition. It is timely that the federal government is identifying such significant impediments to freer trade as non-tariff barriers, currency relationships and domestic legislation on competition.

In the matter of pollution, the company is committed to the requirements of bringing industrial pollution to socially acceptable levels. We are implementing anti-pollution programs on a mill-by-mill basis. The government authorities involved in these programs have recognized the impact which research and technology can play in reducing the total capital and operating costs of pollution abatement projects. The continued government support of extensive research into pollution abatement techniques is of great importance.

The opportunity exists for the industry, as for Domtar, to work with government and labour to ensure that Canadian pulp and paper products are made cost and price competitive on a world-wide basis while generating sufficient funds and attracting necessary outside investment to maintain a healthy and expanding industry.

This achievement will be a major factor in ensuring that the Canadian economy will continue to develop.

Principal Products:

Domtar Fine Papers Ltd. — *Uncoated and coated fine papers for the printing, business and converter trades, as well as specialty papers such as diazo base, glassine, greaseproof, cigarette and carbonizing.*

Domtar Newsprint Limited — *Standard and specialty newsprint; coated publication grade and directory papers.*

Domtar Packaging Limited — *Linerboard, corrugating medium, kraft papers and boxboards for conversion; corrugated shipping containers; packaging and wrapping papers for the consumer trades; grocery and other paper bags; towelling and tissue products; fibre cans and tubes.*

Domtar Pulp Limited — *Bleached and unbleached softwood and hardwood sulphate pulp; semi-bleached softwood sulphate pulp; unbleached sulphite pulp.*

Domtar Woodlands Limited — *Lumber.*

PICTORIAL REVIEW

1. This tree-length harvester at Lebel-sur-Quévillon, Quebec, was one of the first of its kind to be used in Canada. It is capable of felling, limbing and topping one tree every 55 seconds.

2. The hundreds of circuits in this telephone cable are each insulated with Domtar pulp of outstanding quality and strength. The unusual qualities of the pulp used in this sophisticated application are imparted to it by a combination of skilled craftsmanship and the long, slender fibres of the slow-growing, dense black spruce which grows in the vicinity of Lebel-sur-Quévillon, Quebec.

3. The Jim Mathieu Lumber sawmill, near Atikokan in Northwestern Ontario, was integrated into the Woodlands operations during 1972.

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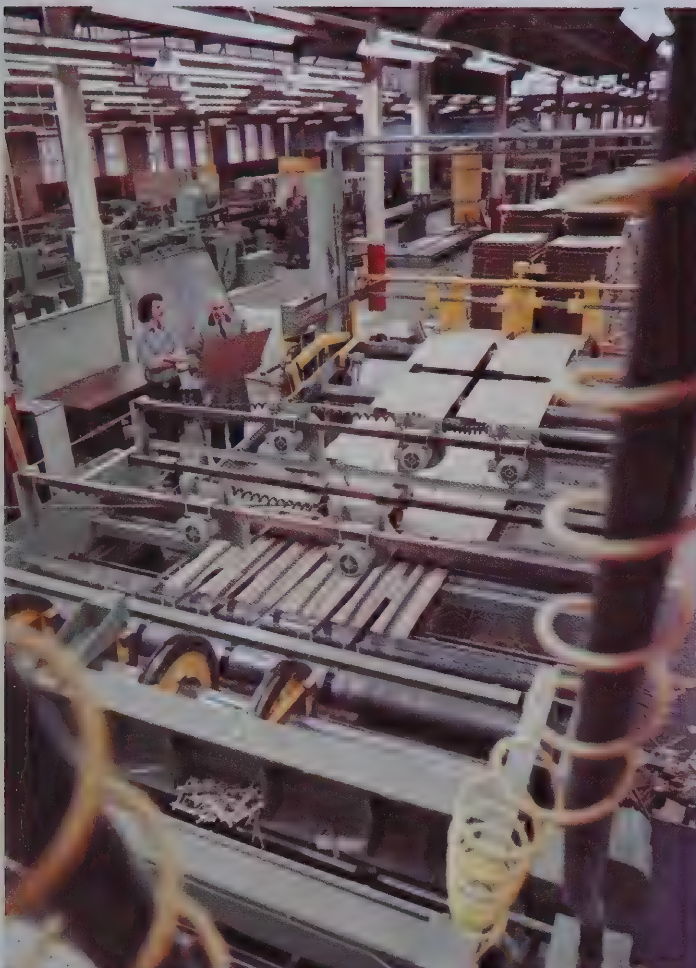
1. Domtar is now a major supplier of paper to the expanding pocket book market. The paper used in these and similar applications is obtained from pulp especially bleached in a plant with related facilities installed at a total cost of some $2 million at Donnacona, Quebec. Henri Marcotte monitors its control centre as Ken Wilkinson checks one of the vacuum thickeners.

2. The recycling of waste materials at the Fine Papers mill in Cornwall, Ontario: here paper waste is fed into the pulper in the de-inking plant by Donald Rupert. The ink is removed by washing and the pulp fibres go to the bleaching plant.

2



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1. The Packaging company's 15th converting plant — with entirely new equipment installed late in 1972 — is well on the way towards full operation. The plant, manufacturing corrugated containers, is located in Leaside, Ontario.

2. A new production line especially designed to make corrugated containers for large appliances and other one-piece oversize packages, similar to those shown here, has been installed in the Packaging plant in Etobicoke, Ontario.

3. The installation of this automatic, high-speed precision paper sheet cutter was another step in making the Sunderland Mill one of the foremost specialty paper mills in the United Kingdom.

4. Donald Brownlee operates the laboratory pulping unit at the Research Centre in Senneville, Quebec. Uses include the development of new pulping processes and the evaluation of new raw materials.

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1. Arborite® decorative laminate graces this striking mural by Montreal artist Guy Montpetit in the lobby of the new Canadian Broadcasting Corporation building in Montreal.

2. Plenair® landscape partition screens, made by Domtar Construction Materials Ltd., add beauty to an office setting with the utmost in flexibility. They are available in straight or curved lengths up to six feet high by six feet wide.

3. When the expansion of the rock salt mine in Goderich, Ontario, is completed in the spring of 1973, it will become one of the largest in North America with an annual capacity of 2.25 million tons a year.

4. Sifto® salt, a product of Domtar Chemicals Limited, meets with increasing consumer acceptance across Canada.

®Registered Trade Mark

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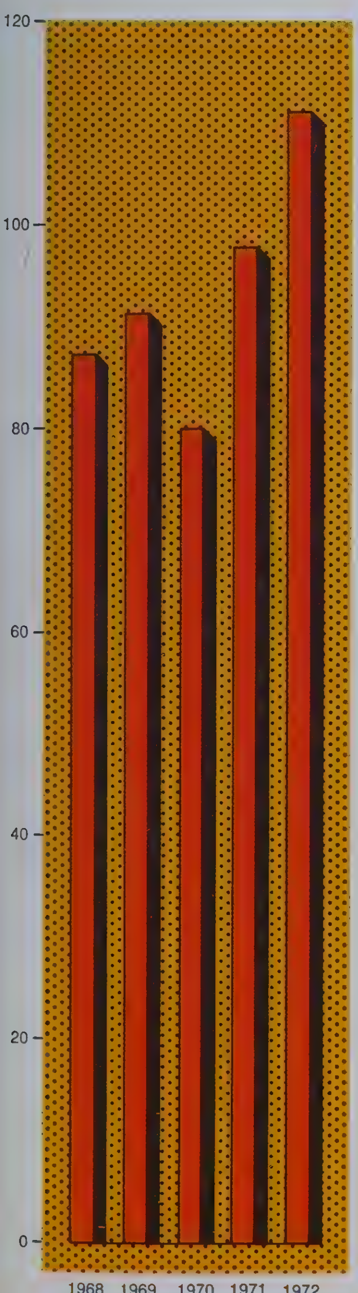
DOMTAR CONSTRUCTION MATERIALS LTD.

Construction Materials Sales
(millions of dollars)



The 1971 upswing in performance continued unabated throughout 1972 with sales recording a sharp advance to a record level of about $111 million.

The ready supply of residential mortgage funds, particularly through the chartered banks and trust companies, enabled the residential construction industry to achieve a record year. Housing starts, at about 250,000 units; completions, with 235,000 units projected; and expenditures, with $5.3 billion indicated; all reached record levels in 1972. An unprecedented number of Canadians were thus able to achieve their personal aspiration of home ownership, whether of a single family unit or, increasingly, a condominium or a townhouse. Coupled with this high level of activity, particularly during the second half of the year, commercial and industrial building construction made significant gains. In dollar value, total building contract awards were 22% higher than in 1971 — the equivalent of a 14% increase in physical volume after taking inflation into account. Because of this unprecedented demand, many of our facilities, as well as those of our suppliers, were stretched beyond capacity with resultant shortages in several product lines.

While an encouraging increase was again registered in operating profit, this was principally due to increased volume as overall unit manufacturing profit margins remained relatively constant. Current profits were adversely affected by the four month strike in our Siporex plant at Delson and the subsequent decision to discontinue production of this product line. These operations, for the production of lightweight cellular concrete products, had not been profitable for several years and, even though the product line had recently been substantially revamped, there was no evidence that a positive contribution could be made to the company within a reasonable period.

The current outlook, at least for the first half of 1973, has to be one of optimism. At the beginning of the year, a record number of housing units were under construction and the commercial and industrial building construction program was active. Mortgage money continues in ready supply. As early as the fall of 1972, lenders were soliciting builders and arranging block funding for 1973 housing programs. Newly completed and unoccupied housing units, notwithstanding record completions, show no significant increase and many builders report strong advance sales for spring delivery.

The housing industry, however, does face three major problems: the shortage of serviced land, a labour shortage and a demand for materials in excess of current manufacturing capacity. Materials manufacturers, including our company, appear to be well on the way to expanding production capacities, many on the premise that the accelerated depreciation allowances and the reduced tax rate for manufacturers announced in the Federal Budget last May will be ratified. The company's gypsum wallboard facilities at Montreal East, Quebec, and Caledonia, Ontario, are being expanded and a separate production line for saturated felt is being installed at Lachine, Quebec. The labour shortage in the construction industry defies logical analysis, particularly in view of the persistently high level of unemployment in Canada. The shortage of serviced land in the majority of urban centres across the nation, which has led to rapid price escalation, has been well established as the major contributing factor to rising housing costs. Co-ordinated government action at all levels to expand major trunk services, thus reducing land speculation, and to ease the property tax burden is essential to adequate housing. Land banking as proposed by several government agencies can, as already demonstrated in various parts of the country, result in literal sterilization of land rather than development. The recent changes to the National Housing Act regulations authorizing higher loans and an increase in the maximum gross debt service ratio (the ratio of the carrying charges for principal, interest and taxes to the gross income of the borrower) from 27% to 30% are indications of positive government action which will undoubtedly assist the industry in meeting the government's stated housing objective. The industry looks forward to early implementation of the announced NHA changes incorporating the Neighbourhood Improvement Plan and the Residential Rehabilitation Assistance Program to eliminate the blight areas in our urban communities. The proposed Assisted Home Ownership Program through federal low cost loans, geared to income and matching federal-provincial government grants, to permit low income families to become home owners as an alternative to public housing is considered to be a positive innovation and should receive wide government and public support.

The major problem facing all segments of the construction industry continues to be the cyclical nature of the business. While there are no short term solutions to this problem, the current study of the industry by the Economic Council of Canada hopefully will indicate the means by which more stable growth can be achieved.

Despite current industry problems, projections for 1973 are for a continued strong market demand with a minor increase in sales and maintenance of earnings.

Principal Products:
Clay brick; acoustical plasters; fibre conduit; NO-CO-RODE® sewer and drainage pipe; asphalt shingles; roll roofing and siding; roof, sheathing and panel board and CEL-U-CON® 25 noncombustible roofboard; ceiling tiles and grid panels; linear ceiling systems; partition systems; gypsum lath, plank and wall board and wall panelling; ARBORITE® decorative and industrial plastic laminates; HAYDITE® lightweight aggregate; plastic conduit.

®Registered Trade Mark

DOMTAR CHEMICALS LIMITED

The historical upward trend continued with 1972 sales 6% above the 1971 level. A modest improvement in operating profit was achieved. The adverse effects of increased costs, some price reductions and non-recurring expenses associated with the closure of two plants were offset by efficiency improvements in some operations and a favourable product mix in others.

Heightened competition from domestic and new foreign sources caused price erosion in some major markets of the Sifto Salt division. Although sales were maintained, operating profit fell below the 1971 level. The division plans to market rock salt on a direct basis in the United States in 1973. To this end, an office located in Schiller Park, Illinois, a suburb of Chicago, was opened and a marketing organization established during the year. In addition to marketing products originating in Canada, the division will participate in new markets for rock salt to be supplied from sources in the United States. The development of new salt products and a continuing program of upgrading packaging has materially assisted the division in several markets. A current example is the establishment of manufacturing facilities at Goderich for the production of portion packs, a growth area in the food industry. Engineering and feasibility studies on a major investment in production facilities on Cape Breton Island in Nova Scotia continue.

The Lime division benefited from the buoyant activity in the Canadian and United States steel industries during 1972. The market for lime used in water and effluent treatment is increasing and the division is providing technical information and services in this field. West Coast operations in Canada and the United States were adversely affected by lower cement stone shipments and extreme pricing pressures. Sales to the construction industry were a little higher than in the previous year. In summary, the division showed a significant improvement through the efficient utilization of recently installed equipment and a strong marketing effort.

Sales of the Wood Preserving division reached a new high, exceeding the previous year by 6%. Operating profit, however, was somewhat lower than in 1971. Results were adversely affected by shortages of raw materials and high costs of wood and labour. The sales gains achieved during the year were primarily due to a stronger Prairie farm market, increased wharf construction in the Atlantic region and higher demand for utility distribution poles in several areas. Railway treating volume declined because the supply of cross ties failed to attain anticipated levels. Heavy emphasis on research and development continued throughout the year and significant progress was made in developing new wood treatments and fire retardant formulations.

Results of the Tar & Chemical division were better than last year but did not meet expectations. A decline in demand for coal tar pitch in the aluminum industry, combined with the higher than planned costs of closing the Toronto chemical plant, were the major influencing factors. Expansion of the Hamilton tar distillation plant announced last year is nearing completion and operations will be under way by about the beginning of the second quarter of 1973.

In the Metal Powders division, an explosion and fire occurred at the Ridgway, Pennsylvania plant on September 5, 1972. In view of the uneconomic pricing situation which still prevails in the iron-based powder business in North America, it has been decided to put the plant up for sale. The Canadian plants at Lachine and LaSalle, Quebec, will continue to supply the market with high quality powders.

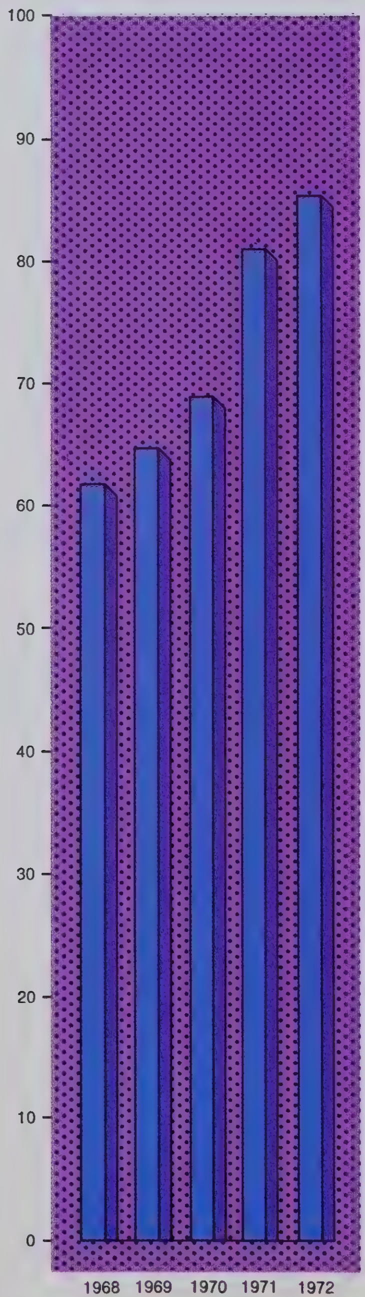
Chemical Developments of Canada Limited had a record year in 1972. There was a strong and sustained demand for all product lines, particularly surfactants and chemical specialties. Several new products were developed. The volume of resale chemicals and dyestuffs also increased in all major consuming industries which include soaps and detergents, pulp and paper and textiles.

Domtar Chemicals Limited enters 1973 on a stronger base due to new and enlarged production facilities and the elimination of unprofitable operations. Sales for the year will depend on the continued demand generated by such basic industries as steel, aluminum, transportation, public utilities and industrial chemicals. Profit improvement will be limited by manpower, fuel and other cost increases in view of the fact that only modest price increases are anticipated.

Principal Products:
SIFTO® salt; pressure treated and fire retardant wood; coal tar pitches and acids; creosote; naphthalene and phthalic anhydride; limestone; hydrated lime and quicklime, iron alloy powders; synthetic detergents; wetting agents; carboxy-methylcellulose; dyestuffs and pigments.

®Registered Trade Mark

Chemical Sales
(millions of dollars)



CONSOLIDATED STATEMENT OF NET INCOME

Year ended December 31

	1972	1971
Sales and revenues:		
Sales	$560,779,334	$516,376,401
Investment and sundry income	1,419,499	2,976,089
	562,198,833	519,352,490
Costs and expenses:		
Cost of sales and selling and administrative expenses	496,035,388	464,420,374
Depreciation	26,431,640	26,107,049
Interest on funded debt	7,637,113	8,239,075
Interest on other indebtedness	250,970	294,587
	530,355,111	499,061,085
Income before income taxes, minority interest and extraordinary items	31,843,722	20,291,405
Current income taxes	8,320,000	4,550,000
Deferred income taxes	5,255,000	4,430,000
Minority interest	800,935	810,966
	14,375,935	9,790,966
Income before extraordinary items	17,467,787	10,500,439
Extraordinary items	4,100,000	8,700,000
Net income for the year	$ 13,367,787	$ 1,800,439
Earnings per common share before extraordinary items	$1.14	$0.67
Earnings per common share after extraordinary items	$0.86	$0.08

CONSOLIDATED STATEMENT OF EARNED SURPLUS

Year ended December 31

	1972	1971
Earned surplus, balance at beginning of year	$ 95,136,085	$102,824,772
Net income for the year	13,367,787	1,800,439
	108,503,872	104,625,211
Dividends on —		
Preference shares ($1 per share)	592,746	592,746
Common shares ($0.60 per share)	8,896,380	8,896,380
	9,489,126	9,489,126
Earned surplus, balance at end of year	$ 99,014,746	$ 95,136,085

See accompanying notes to financial statements.

CONSOLIDATED BALANCE SHEET

December 31

Assets

	1972	1971
Current assets:		
Cash and short-term investments	$ 11,683,729	$ 11,427,106
Receivables	95,750,392	84,369,027
Inventories, at lower of cost and net realizable value	85,218,804	87,465,780
Prepaid expenses	1,717,621	1,840,786
	194,370,546	185,102,699
Investments and advances, at cost:		
Listed securities (quoted value $9,482,000; 1971 — $5,128,000)	13,319,969	13,319,969
Other investments and advances	13,062,013	11,856,244
	26,381,982	25,176,213
Fixed assets, at cost:		
Plant, machinery and facilities	625,131,044	613,674,258
Timber limits and land	26,699,937	26,262,614
	651,830,981	639,936,872
Less: Accumulated depreciation	356,015,028	340,221,325
	295,815,953	299,715,547
	$516,568,481	$509,994,459

APPROVED BY THE BOARD:

T. N. Beaupré, Director

C. W. Webster, Director

Liabilities

	1972	1971
Current liabilities:		
Bank indebtedness	$ 1,891,313	$ 2,036,835
Payables	54,766,372	47,907,017
Income and other taxes	4,968,010	1,459,556
Dividends payable	2,505,750	2,363,564
Funded debt due within one year	—	7,115,000
	64,131,445	60,881,972
Funded debt	123,023,000	127,098,000
Deferred income taxes	71,331,000	67,503,000
Minority interests	12,394,937	12,702,049
Capital:		
Capital stock —		
$1 cumulative redeemable preference shares, par value $23.50, redeemable at $25 —		
Authorized — 600,000 shares		
Outstanding — 592,746 shares	13,929,531	13,929,531
Common shares without nominal or par value —		
Authorized — 25,000,000 shares		
Outstanding — 14,827,300 shares	132,743,822	132,743,822
Earned surplus	99,014,746	95,136,085
	245,688,099	241,809,438
	$516,568,481	$509,994,459

See accompanying notes to financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1972

1. Consolidation:

The accompanying financial statements include the accounts of Domtar Limited and all its subsidiary companies.

Current assets and current liabilities in foreign currencies have been translated into Canadian dollars at current rates of exchange at December 31, 1972. Fixed assets and other long-term assets and liabilities have been translated at rates of exchange in effect at the dates of the transactions.

2. Extraordinary items:

The Company has closed the Siporex plant at Delson, Quebec, and has put up for sale the Metal Powders plant at Ridgway, Pennsylvania, which was partially destroyed by fire. The Company has also decided to provide for the write-off of certain idle facilities which form part of the mill at Red Rock, Ontario.

After giving effect to deferred income taxes of $1,427,000, the appropriate depreciation and estimated realizable values, the extraordinary losses amounted to $4,100,000.

3. Inventories:

	December 31 1972	December 31 1971
Logs and pulp chips	$13,705,698	$19,704,477
Raw materials and operating and maintenance supplies	33,490,106	32,050,303
Finished goods including work-in-process	38,023,000	35,711,000
	$85,218,804	$87,465,780

4. Other investments and advances:

	December 31 1972	December 31 1971
Secured loans to the Trustees for employees under the Company's stock purchase plan	$ 1,440,726	$ 1,781,294
Municipal bonds	6,102,000	6,276,000
Loans, mortgages and debentures	5,085,209	3,236,363
Shares	434,078	562,587
	$13,062,013	$11,856,244

5. Fixed assets:

	Cost	Accumulated depreciation	Net book value
	(millions of dollars)		
December 31, 1972 —			
Plant, machinery and facilities —			
Pulp and paper	$455.4	$237.0	$218.4
Construction materials	81.6	58.6	23.0
Chemicals	82.8	51.2	31.6
Other	5.3	4.5	.8
Timber limits and land	26.7	4.7	22.0
	$651.8	$356.0	$295.8
December 31, 1971 —			
Plant, machinery and facilities —			
Pulp and paper	$442.4	$223.9	$218.5
Construction materials	82.7	58.1	24.6
Chemicals	82.7	49.3	33.4
Other	5.9	4.2	1.7
Timber limits and land	26.2	4.7	21.5
	$639.9	$340.2	$299.7

6. Funded debt:

	Maturity	December 31 1972	December 31 1971
Domtar Limited —			
Sinking fund debentures —			
5¼ % Series "A"	1978	$ 12,500,000	$ 12,500,000
6¼ % Series "B"	1980	7,575,000	7,575,000
5½ % Series "C"	1982	12,200,000	12,200,000
5¾ % Series "D"	1984	14,400,000	14,400,000
5⅝ % Series "E"	1990	35,000,000	35,000,000
6¾ % Series "F"	1987	35,000,000	35,000,000
St. Lawrence Corporation Limited —			
First mortgage sinking fund bonds —			
5% Series "A"	1972	—	5,357,000
4¾ % Series "B"	1972	—	1,948,000
5% Series "C"	1978	5,876,000	6,428,000
Sinking fund debentures —			
6¾ % Series "A"	1980	11,400,000	11,400,000
		133,951,000	141,808,000
Less: Held for sinking fund		10,928,000	7,595,000
		123,023,000	134,213,000
Balance of instalments due within one year included in current liabilities		—	7,115,000
		$123,023,000	$127,098,000

Approximate instalments due in each of the next five years: 1973 — nil; 1974 — $2,426,000; 1975 — $8,077,000; 1976 — $8,077,000; 1977 —$8,077,000.

7. Minority interests:

	December 31 1972	December 31 1971
Preferred shares of subsidiary company:		
St. Lawrence Corporation Limited — 100,136 5% preferred shares of $100 each, redeemable at $101 (after purchase for redemption during the year of 4,139 shares)	$10,013,600	$10,427,500
Common share equity in subsidiary companies	2,381,337	2,274,549
	$12,394,937	$12,702,049

8. Pension fund:

The Company and its subsidiaries have pension plans for their employees. These plans have been amended effective January 1, 1973 to permit retirement at full pension at age 62 under certain conditions. After giving effect to this amendment, the unfunded past service pension liability at December 31, 1972 approximates $13,632,000 and is being funded over the next eighteen years as recommended by the actuaries.

9. Information on directors and officers:

	Number Year ended December 31 1972	Number 1971	Remuneration Year ended December 31 1972	Remuneration 1971
Directors	19	20	$ 84,725	$ 84,491
Officers	22	24	1,040,355	974,622
Officers who are also directors	1	1		

10. Sales by class of business:

	Year ended December 31 1972	1971
	(millions of dollars)	
Pulp and paper products	$ 364.5	$ 338.5
Construction materials	110.9	97.7
Chemicals	85.4	80.2
	$ 560.8	$ 516.4

CONSOLIDATED STATEMENT OF SOURCE AND APPLICATION OF FUNDS

Year ended December 31

	1972	1971
Source of funds:		
Net income	$ 13,367,787	$ 1,800,439
Depreciation	26,431,640	26,107,049
Deferred income taxes	5,255,000	4,430,000
Extraordinary items, not affecting working capital	4,526,000	8,700,000
Cash flow from operations	49,580,427	41,037,488
Application of funds:		
Fixed assets	28,485,046	23,655,786
Funded debt	4,075,000	14,873,000
Minority interest	307,112	2,079,329
Investments and advances	1,205,769	(1,436,162)
Dividends on preference shares	592,746	592,746
Dividends on common shares	8,896,380	8,896,380
Amalgamation expenses	—	180,296
	43,562,053	48,841,375
Increase (decrease) in working capital	6,018,374	(7,803,887)
Working capital at beginning of year	124,220,727	132,024,614
Working capital at end of year	$130,239,101	$124,220,727

See accompanying notes to financial statements.

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of Domtar Limited and its subsidiaries as at December 31, 1972 and the consolidated statements of net income, earned surplus and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the consolidated financial position of the companies as at December 31, 1972 and the results of their operations and the source and application of their funds for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Montreal, January 29, 1973

Price Waterhouse & Co.
Chartered Accountants

HISTORICAL REVIEW

Financial	1972	1971	1970	1969	1968	1967	1966
				(millions of dollars)			
Net fixed assets	**295.8**	299.7	304.1	290.9	291.3	306.2	316.0
Net working capital	**130.2**	124.2	132.0	146.7	143.7	118.3	77.7
Investments and advances	**26.4**	25.2	34.4	36.4	34.0	52.5	27.1
Total net assets	**452.4**	449.1	470.5	474.0	469.0	477.0	420.8
Represented by:							
Funded debt	**123.0**	127.1	142.0	147.1	155.7	165.4	137.2
Deferred income taxes	**71.3**	67.5	64.1	53.7	51.6	52.4	47.8
Minority interest	**12.4**	12.7	22.1	23.0	24.0	25.1	26.1
Shareholders' equity	**245.7**	241.8	242.3	250.2	237.7	234.1	209.7
	452.4	449.1	470.5	474.0	469.0	477.0	420.8
Sales and Revenues:							
Pulp and Paper	**364.5**	338.5	335.7	310.1	279.0	272.0	272.3
Chemicals	**85.4**	80.2	68.7	64.0	62.0	57.5	56.3
Construction Materials	**110.9**	97.7	80.5	90.7	86.4	81.0	84.1
Consumer Products	**—**	—	—	—	—	17.5	17.4
Other revenues	**1.4**	3.0	6.7	7.2	4.7	2.0	2.0
	562.2	519.4	491.6	472.0	432.1	430.0	432.1
Income before taxes	**31.0**	19.5	26.9	32.0	20.7	14.9	30.3
Current income taxes	**8.3**	4.6	10.4	9.9	8.6	6.0	4.0
Deferred income taxes	**5.3**	4.4	(1.1)	2.1	(0.7)	0.1	10.6
Net income	**17.4***	10.5*	17.6	20.0	12.8	8.8	15.7
Cash flow	**49.6**	41.0	42.8	47.1	37.1	31.3	48.2
Capital expenditures	**28.5**	23.7	39.0	24.6	10.1	16.4	57.6
				$ Per Common Share			
Earnings	**1.14***	0.67*	1.17	1.33	0.85	0.58	1.04
Dividends	**0.60**	0.60	0.70	0.60	0.60	0.90	1.00
Cash flow	**3.30**	2.73	2.86	3.16	2.51	2.11	3.27
Book value	**15.63**	15.37	15.87	16.40	15.69	15.49	13.82

*Before deducting extraordinary items of $4.1 million (1971 — $8.7 million) or $0.28 per common share (1971 — $0.59).

Pulp and paper production (Tons)							
Newsprint	**380,749**	467,791	480,114	542,434	520,127	521,856	586,976
Kraft Paper and Board	**433,664**	420,878	413,883	388,675	364,800	388,912	378,394
Fine and Specialty Papers	**328,495**	321,803	299,998	250,380	214,700	204,525	207,572
Market Pulp	**265,600**	223,300	297,400	294,800	221,700	223,683	191,868
	1,408,508	1,433,772	1,491,395	1,476,289	1,321,327	1,338,976	1,364,810

The cover of this Annual Report was
lithographed in Canada on Domtar
"Byronic" Text Cover, Britewhite,
brocade finish, 160(M). The inside pages
were lithographed on Domtar "Luxagloss"
Offset Enamel, White, 200(M).